



County of Los Angeles CHIEF ADMINISTRATIVE OFFICE

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DAVID E. JANSSEN
Chief Administrative Officer

December 7, 2004

To: Supervisor Gloria Molina, Chair
Supervisor Yvonne B. Burke
Supervisor Zev Yaroslavsky
Supervisor Don Knabe
Supervisor Michael D. Antonovich

From: David E. Janssen
Chief Administrative Officer

Board of Supervisors
GLORIA MOLINA
First District

YVONNE B. BURKE
Second District

ZEV YAROSLAVSKY
Third District

DON KNABE
Fourth District

MICHAEL D. ANTONOVICH
Fifth District

THE DISTRIBUTION OF PROPOSITION 1A FUNDS

On November 16, 2004, Supervisor Antonovich requested that my office report to your Board with recommendations on the distribution of Proposition 1A funds. While the County will not receive any new funding as a result of Proposition 1A, there will be an increase in available County funds in 2006 as a result of Proposition 1A's requirements that the State pay back the monies it borrowed from local governments in the FY 2003-04 and FY 2004-05 budget years. This report describes those funds and their anticipated availability for County budgeting.

Vehicle License Fee (VLF) Gap Loan

In June 2003, when then Governor Davis announced that the State could no longer afford to pay local governments the VLF backfill and that he would allow the statutory trigger mechanism to restore the rate to its original 2 percent level, a little over three months elapsed before the increase could be implemented. During that period, local governments went without \$1.2 billion in VLF revenue. In return for this contribution to the FY 2003-04 State budget solution, local governments were guaranteed in law that the "VLF gap loan" would be repaid in August 2006. **Los Angeles County's share of the loan is \$204.7 million.** Because the repayment date is in statute, it can be changed by the Legislature to delay repayment or even eliminate it entirely. However, included among Proposition 1A's constitutional changes is a provision intended to insure State repayment by making any future State borrowing of local property tax revenue contingent on repayment of the gap loan.

To remove this uncertainty, on December 7, 2004, your Board approved the securitization of the State's obligation by which the County will sell the gap loan proceeds to two banks which will assume the risk of a delay or non-payment. In return, the County will accept a reduced amount of either \$193.5 million, or \$188 million if the State fails to repay the loan in August 2006.

The receipt of the proceeds from securitization of the gap loan will result in a one-time windfall for the County general fund, as Attachment A illustrates. Because the notes are tax free, the proceeds must be used for capital improvements. My office is preparing a list of projects for your approval.

Deferred Mandate Payments

Starting in FY 2002-03, the State stopped reimbursing local governments for most State-mandated services, including amounts owed from prior years. As part of last year's agreement with local governments that included Proposition 1A, the State agreed to cease any further deferrals and to begin paying the accumulated debt over five years, beginning with the Budget Act of 2006-07. The statute does not stipulate how the money will be repaid, for example, whether the payments will be in five equal installments. **Los Angeles County's share of deferred mandates will reach approximately \$272 million at the end of the current budget year.**

The repayment of these funds will effectively reimburse the County General Fund for services that have been provided over the past three years using County monies. Since the funds are a receivable to the department that provided the services, they will be credited to the department for the year in which they are received. At year-end closing, those departments could have excess funds that would become part of the balance forward. At that time, the Board will have to decide on their use in light of the priorities and needs at that time. However, since this funding stream is uncertain and will end after five years, it would not be advisable to count on these funds for ongoing programs.

VLF-Property Tax Swap

As part of last year's agreement between local governments and the State, local governments agreed to give up the VLF backfill in return for an equal amount of property taxes. However, in FY 2004 and FY 2005, local governments collectively agreed to give up \$1.3 billion in property taxes as their contribution to the State budget solution. **Los Angeles County's General Fund share of that amount is \$103.2 million for each year.** (Special districts administered by the Department of Public Works also contributed approximately \$10 million.) Starting in 2006 this amount will automatically be restored to the County's property tax base.

The restoration of \$103.2 million in property taxes will improve the County's revenue base to what it would have been had the State not taken these funds for two years, as Attachment B illustrates. Because the County will use one-time fund balance to backfill their loss, the reimbursement is not new money and should not be counted on to fund new or expanded programs in FY 2006-07.

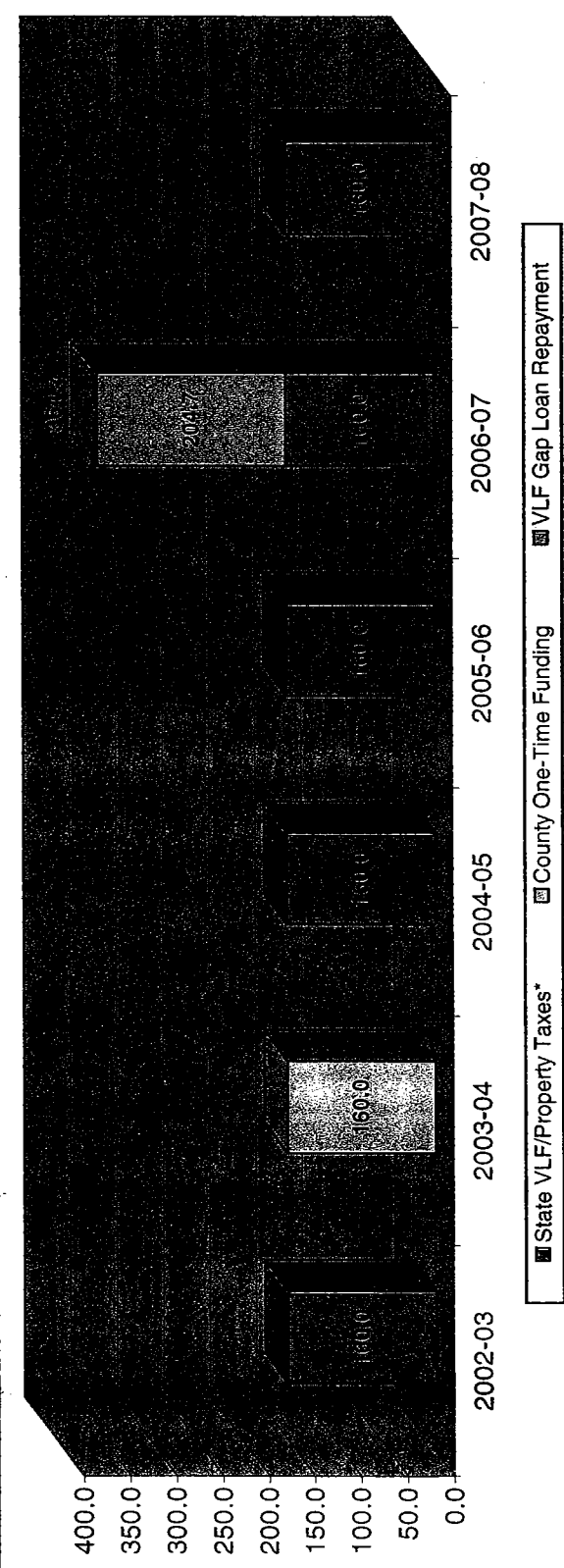
Given the fact that State budget deficits are projected for the foreseeable future, I believe your Board should be cautious about committing these or other revenues until we know what actions the State takes to balance its budget in 2005 and 2006.

DEJ:GK
MAL:JR:ib

Attachments

c: Executive Officer, Board of Supervisors
 County Counsel
 Auditor-Controller

Vehicle License Fee (VLF) Gap Funding Summary
(in millions)



2002-03

■ - Reflects approximately 23.5% of the total VLF budget and the projected 03-04 3-month VLF backfill loss.

2003-04

■ - Reflects one-time funding utilized to offset the one-time projected 3-month VLF loss of \$160.0 million. State to repay County in August 2006 as stipulated in the Local Government Agreement.

2004-05

■ - Reflects the initial year of the two-year dollar for dollar swap of VLF for Property Tax revenues under the Local Government Agreement.

2005-06

■ - Reflects the second year of the two-year dollar for dollar swap of VLF for Property Tax revenues under the Local Government Agreement.

2006-07

■ - Reflects the permanent substitution of VLF revenues for Property Taxes.
■ - Reflects the State pay back of the 03-04 3-month VLF backfill loss adjusted to reflect \$204.7 million actual loss reported by the State. Amount will be reduced if County securitizes due to cost of borrowing.

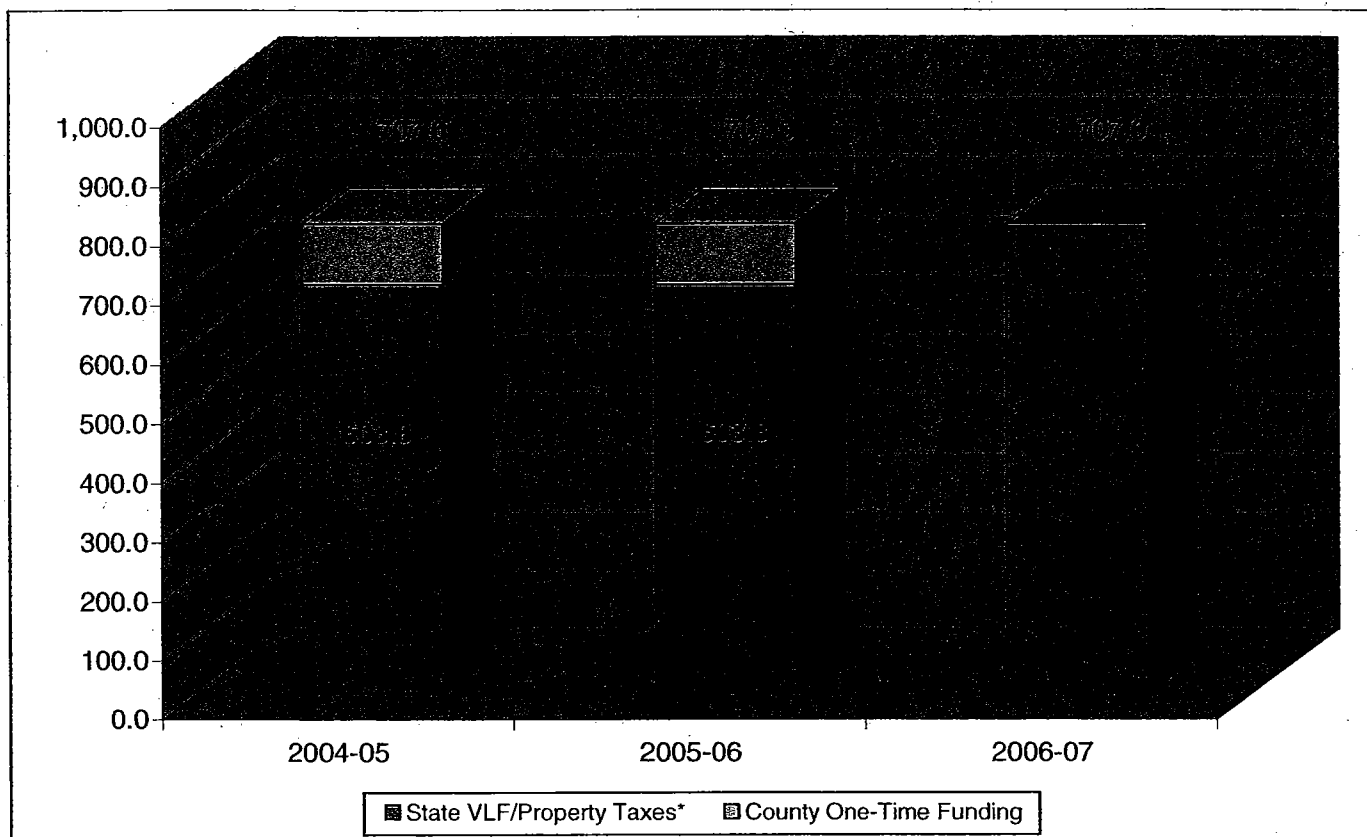
2007-08

■ - Reflects the permanent substitution of VLF revenues for Property Taxes.

* Reflects substitution of VLF revenue for a like amount of Property Tax revenue effective July 1, 2004.

Local Government Agreement Shift Impact

(in millions)



2004-05

- -The County's loss of revenue that provided the 04-05 contribution of \$103.2 million to the State was funded on a one-time basis from: Child Support Automation Penalty 11.0 million, PFU-DPSS Food Stamp Error \$81.1 million, and Fund Balance \$11.1 million.
- -The 04-05 Proposed Budget reflected a Vehicle License Fee- Regular Budget of \$707.0 million prior to the Local Government Agreement.

2005-06

- -The 05-06 Proposed Budget reflects the second year of the County's \$103.2 million contribution to the State which was funded with one-time excess 2003-04 Fund Balance.
- -If not for the Local Government Agreement, revenue was projected at \$707.0 million.

2006-07

- -Reflects the permanent shift of projected VLF revenues to Property Tax budget to restore the full \$707.0 million in funding prior to the Local Government Agreement; therefore resulting in no new ongoing revenues.

* Reflects substitution of VLF revenue for a like amount of Property Tax revenue effective July 1, 2004.